

DEPARTMENT OF WATER RESOURCES

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Counter-Proposal**State Water Project – Contract Extension
Proposed Agreement in Principle****1 OBJECTIVE 1: TERM OF CONTRACT**

- a. Extend term of the SWP water supply contracts by 40 years from December 31, 2035 to December 31, 2075.

2 OBJECTIVE 2A: RESERVES**2.1 Funding Level for General Operating Account (GOA)**

- a. Equivalent to 90 days' worth of operating reserves (\$150 million in today's dollars) built-up over time based on the phased increases in GOA funding levels outlined in DWR Section 2.9.b. Increase the authorized General Operating Account (GOA) balance from \$22.7 million to \$150 million pursuant to Article 51(a)(3)¹. Authorized GOA funding level will be adjusted as outlined in DWR Section 2.9.c.
- b. The GOA funding level shall be based on 90 days' worth of operating reserves. Changes in authorized GOA funding will be based on a periodic review by DWR and the Contractors.
- c. The initial funding source for pre-2035 adjustments to the authorized GOA funding level will be 51(e) revenues and a transfer from the Replacement Accounting System (RAS) account.
- d. The funding source for post-2035 adjustments to the authorized GOA funding level will be at the discretion of the Director:
 - (1) investment earnings retained in GOA;
 - (2) transfers from the SWRDS Reinvestment Account (SRA); and

¹ The Articles referenced in this document are articles contained within the SWP water supply contracts.

- (3) any other available funds.

2.2 Funding Rate for GOA

- a. Subsequent to the payoff of the Pooled Money Investment Account (PMIA) loan, change the authorized GOA funding rate of \$2 million annually, to any amount of available revenues determined in Article 51(e)(1)(ii) subject to the phased funding increases set out in the contract provisions and authorized maximum GOA funding level.

2.3 Funding Priority for GOA

- a. Subsequent to the payoff of the Pooled Money Investment Account (PMIA) loan, the GOA funding priority established by the post-Monterey flow of funds would be modified to establish GOA funding subordinate to rate reductions under Article 51(e)(1)(ii).

2.4 Replenishment of the GOA

- a. Authorize the replenishment of the GOA through the normal statement of charges process pursuant to Article 29 (e), under the billing component that represents the costs incurred which triggered the event requiring the use of the GOA.

2.5 Interest Earnings on the GOA

- a. GOA investment earnings shall be used as follows:
 - (1) funding GOA to authorized GOA funding level;
 - (2) transferred, at the discretion of the Director, to the SWRDS Support Account (SSA); and
 - (3) transferred, at the discretion of the Director, to the SWRDS Reinvestment Account (SRA).

2.6 Uses of the GOA

- a. Authorize the GOA to be used for any cash-flow deficiencies resulting from a chargeable water supply purpose within the SWRDS or during a SWRDS emergency for any SWRDS purpose.

2.7 Other Cash-flow Mitigation Measures

- a.
 - (1) Retain the supplemental billing provisions authorized under Article 51(c)(4) prior to January 1, 2036, and, for post-2035, allow supplemental billing up to 10% of the Contractors' current Statement of Charges for that calendar year.

- (2) Effective with the new amended contract, DWR shall have the ability to issue “revised” Contractor billings in the event of a significant cash flow shortage caused by an emergency or crisis, where the GOA does not have sufficient funds available or where use of the GOA would deplete the fund and put the State Water Project (SWP) at financial risk.

2.8 Implementing SWRDS Financial Management Enhancements

Enhance the Fiscal Policies and Administrative Measures for the Financial Management of the State Water Resources Development System (SWRDS).

- a. Effective immediately, DWR shall establish a State Water Resources Development System Financial Steering Committee, the structure and responsibilities of which will be described in a Committee Charter approved by DWR as well as the Contractors.

Composition of Committee

- (1) The committee will be comprised of DWR and State Water Project Contractor representatives.
- (2) The Chair of the committee shall be the SWP Deputy Director.

Purpose of the Committee

- (1) To continue development and implementation of the SWRDS Financial Management Enhancements.
- (2) To provide financial recommendations to the Department Director, which include recommendations regarding financial policies, goals, and budgets that support the financial health and viability of the SWRDS.

2.9 Periodic Review and Adjustments

- a. Eliminate the GOA adjustment authorized after 2001 in Article 51(a)(3).
- b. Based on current projections and subject to availability of 51(e) revenues, the GOA will be incrementally increased to the maximum authorized funding level. The CY 2013 initial balance of the GOA is \$27 million, and upon execution of the amended contract, \$20 million shall be transferred from the RAS account. Full funding is projected to be achieved in CY 2017.
- c. Division of Fiscal Services Chief will prepare an analysis of the GOA funding level.

3 OBJECTIVE 2B: SWRDS Support Account (SSA)

3.1 Modifications to Article 51

- a. On January 1, 2036, Article 51 shall no longer be effective, with the exception of Article 51(a) (the General Operating Account) as it may be amended and Article 51(c)(4), (5), and (6) (Supplemental Billing) as they may be amended.
- b. On January 1, 2036, the State Water Facilities Capital Account will cease (Article 51(b)) and the funds in the Facilities Capital Account on that date will be transferred to the SWRDS Support Account.

3.2 SWRDS Reinvestment Account (SRA)

- a. The SRA shall be established and take effect upon the effective date of the contract extension amendment.
- b. The purpose of the SRA shall be to provide a SWRDS revenue stream by reinvesting the SRA balance of Article 51(e)(1)(iii) revenues, collected by the State pre-2035, in facilities and programs that benefit the State Water Project.
- c. Authorized SRA investments shall be as follows:
 - (1) Reinvestment in SWP capital facilities, recovered at the prevailing tax-free municipal bond market rates corresponding to the SWRDS bond rating at the time of financing, in maturity ranges that may extend 10 to 50 years or even to the termination date of the contract extension amendment.
 - (2) Temporary financing in lieu of the SWRDS commercial paper program.
 - (3) Any other legally permissible investment for the SWRDS.
- d. Replenishment or a periodic review of the SRA funding level is not necessary given the nature of the account which is to preserve the SRA balance of Article 51(e)(1)(iii) monies, collected by the State ("principal balance"); insuring that this principal balance can be invested to generate a future revenue stream.
- e. The investment earnings generated by the SRA will, at the discretion of the Director:
 - (1) Provide the annual source of replenishment funds to the State Water Resources Development System Support Account (SSA).
 - (2) For funds not transferred to the SSA, be accumulated in the SRA and increase the SRA balance of Article 51(e)(1)(iii) monies, collected by the State and held in this SRA for investment purposes.

3.3 SWRDS Support Account (SSA)

- a. A SWRDS Support Account (SSA) shall be established, although it is anticipated that the SSA will be used primarily after January 1, 2036.

- b. The purpose of the SSA shall be to provide a source of funds to pay for costs of the System where there are currently no funds or revenue sources available to pay for such costs.
- c. The Department shall consult with and consider input from the Contractors regarding the projects and activities for which monies from the SSA are used.
- d. The initial target amount in the SSA shall be \$60 million, provided that the target amount shall be adjusted up or down every five years based on the percentage change in annual charges to the contractors (or such other formula or index agreed upon by the parties, as part of the contract extension negotiation process).
- e. The Department shall fund the SSA from available System revenues, including Article 51(e)(iii) revenues, the SRA and from the amounts, if any, remaining in the Facilities Capital Account on December 31, 2035, so that the SSA will contain the target amount on January 1, 2036.
- f. Replenishment of the SSA shall be accomplished through:
 - 1) reimbursements received for expenditures made from the SSA;
 - 2) transfers, in the discretion of the Director, from the SRA;
 - 3) transfers, in the discretion of the Director, of investment earnings from the GOA;
 - 4) deposits in the discretion of the Director, from other available system revenues; and
 - 5) interest and other investment income retained in the SSA.
- g. Backstop: If the Department is unable, for any reason, to use the SRA to provide a revenue stream to replenish the SSA or if the SRA is implemented but the SSA is short of funds in any calendar year, then starting no sooner than Calendar Year 2036 (or in any subsequent calendar year where there is a shortage of funds in the SSA), the Department may charge the Contractors annually as follows:
 - (1) 1% of the Contractors' annual charges for the billing year, or
 - (2) a percentage (if less than 1%) of the Contractors' annual charges which, when applied to the amount then in the SSA, will bring the SSA up to the target amount for the billing year.

4 OBJECTIVE 3: Simplify the State Water Project Billing Process

4.1 Elimination of the Replacement Accounting System (RAS)

- a. Eliminate the Replacement Accounting System (RAS) for Transportation and Conservation Facilities, with the intent to have replacement costs treated as a minimum or capital cost, once the maximum authorized GOA funding level has been achieved. DWR will refund the balance less \$20 million of the unencumbered cash balance of the RAS funds to the Contractors using the RAS allocation methodology.

4.2 Implement the Freeze-Go Billing Methodology

- a. Methodology will freeze all costs incurred prior to January 1, 2016, and continue repayment consistent with current contract terms.
- b. Methodology will recover all costs incurred after December 31, 2015, by converting and authorizing repayment on a Pay-As-You-Go methodology.
- c. Amend the definition of the Project Repayment Period to apply only to those costs incurred prior to January 1, 2016.
- d. The term of the Project Repayment Period, January 1, 1961 through December 31, 2035, will remain the same.
- e. The Water Systems Revenue Bond Surcharge will apply only to those costs incurred prior to January 1, 2016 and will terminate at the completion of the Project Repayment Period.
- f. Amend the definition of the Project Interest Rate to apply only to those costs incurred prior to January 1, 2016. The Project Interest Rate will remain 4.610%.
- g. DWR shall have the authority to issue "revised" Contractor billings as needed.

4.3 Defining the Pay-As-You-Go Repayment of Costs Incurred Post-2015

- a. The annual cost recovery within a bill year for estimated annual operation, maintenance, power, and replacement costs for project conservation facilities.
- b. The annual recovery of actual debt service, created by SWRDS financing activities, within a bill year for financed capital transportation and conservation facilities.

4.4 Defining the Pay-As-You-Go Repayment of Actual Debt Service from SWRDS Financing Post-2015 Capital Costs

- a. Authorize SWRDS to finance 100% of all capital costs.
- b. Authorize SWRDS to use various methods of financing including Water System Revenue Bonds and SRA, with each method providing an annual repayment schedule which includes a principal and interest component over the life of the financing.

- c. Authorize SWRDS to bill an amount that is equal to the accumulated annual debt service payments due per the debt service schedules or matching dollar for dollar the SWRDS annual debt service payments including the bond cover requirements, providing 100% capital cost recovery at the financed interest rate over the term of the financing while meeting the additional bond debt cover requirements.

4.5 Expanding Water System Facilities Authorized to be Financed by Water System Revenue Bonds Under Article 1(hh)

- a. Eliminate the January 1, 1987 date for existing facilities within Article 1(hh)(8); provision to now read as follows, " Finance all repairs, additions, and betterments to conservation or transportation facilities and to all other facilities described in this sub-article (hh) except for item (5) the land acquisition prior to December 31, 1995 for the Kern Fan Element of the Kern Water Bank."
- b. Add provision to Expand 1(hh) to include "Finance all other capital projects (i.e. projects and programs for which revenue bonds can be sold) mutually agreed upon in writing by DWR and 80% of the affected Contractors, provided that the approving Contractors' Table A amounts exceed 80% of the Table A amounts representing all affected Contractors". "Affected Contractors" mean those contractors which would be obligated to pay a share of the debt service for such project.